Supreme Court, U.S.
FILED
DEC 15 1989
JOSEPH F. SPANIOL, JR.
CLERK

No. 89-554

In the Supreme Court of the United States

OCTOBER TERM, 1989

HENNEPIN COUNTY, MINNESOTA, ET AL., PETITIONERS

v.

LOUIS W. SULLIVAN, SECRETARY OF HEALTH AND HUMAN SERVICES

ON PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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QUESTION PRESENTED

Whether 42 U.S.C. 1395x(v)(1)(A)(ii) (1982 & Supp. V 1987) imposes a statutory duty upon the Secretary of Health and Human Services to apply retroactively newly promulgated methods for adjusting the amount of reimbursement to which a Medicare health care provider is entitled even though the provider is found not to merit an adjustment under the methods in effect at the time the costs were incurred.

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OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 1a-17a) is reported at 883 F.2d 85. The opinions of the district court (Pet. App. 18a-33a, 35a-37a) are reported at 689 F. Supp. 1.

JURISDICTION

The judgment of the court of appeals wa entered on June 30, 1989. The petition for a writ of certiorari was filed on September 28, 1989. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. Under the Medicare Act, a health care provider is entitled to reimbursement for the lesser of the "reasonable costs" of covered services, as defined under 42 U.S.C. 1395x(v) (1982 & Supp. V 1987), or the provider's customary charge for such services, 42 U.S.C. 1395f(b)(1). In establishing methods for calculating reimbursable "reasonable costs," the Secretary must "take into account both direct and indirect costs to providers of services" to ensure that the actual costs of covered services are reimbursed but that the Medicare program does not absorb the costs of services that are not covered. 42 U.S.C. 1395x(v)(1)(A)(i) (1982 & Supp. V 1987).[1] The Act further provides, in the

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[1] To encourage efficiencies in the delivery of health care services, Congress amended 42 U.S.C. 1395x(v)(1)(A) (1982 & Supp. V 1987) in the Social Security Amendments of 1972 by redefining "reasonable cost" as "the cost actually incurred, excluding therefrom any part of incurred cost found to be unnecessary in the efficient delivery of needed health services." In the same amendments, Congress also authorized the Secretary to promulgate regulations "for the establishment of limits on * * * incurred costs * * * " (*ibid.*). Pursuant to this grant of authority, the Secretary promulgated regulations that fix cost limits for certain items and services furnished by providers. See 39 Fed. Reg. 20,164-20,166 (1974), *adding* 42 C.F.R. 405.460 (1985), *redesignated as* 42 C.F.R. 413.30 (51 Fed. Reg. 34,790, 34,800-34,802 (1986)). (These regulations are referred to in the opinions below in their original codification.)

Section 413.30(f) provides for certain exceptions to the cost limits specified in Section 413.30(a)-(e). In particular, a provider is entitled to seek an upward adjustment of reimbursement for extra costs incurred as a result of its medical education program. See Section 413.30(f)(4). In order to qualify for this adjustment, the provider must show that any indirect medical education costs incurred in excess of the applicable cost limits were "reasonable, attributable to the circumstances specified, separately identified by the provider, and verified by the [fiscal] intermediary." 42 C.F.R. 413.30(f). The provider must also demonstrate that the increased costs attributable to its education pro-

section at issue here, 42 U.S.C. 1395x(v)(1)(A)(ii) (1982 & Supp. V 1987) ("clause (ii)"), that the Secretary shall establish regulations to "provide for the making of suitable retroactive corrective adjustments where, for a provider of services for any fiscal period, the aggregate reimbursement produced by the methods of determining costs proves to be either inadequate or excessive."

2. Petitioner Hennepin County Medical Center (HCMC) is a teaching hospital with a graduate medical education program. Pet. App. 7a. In this action, HCMC and petitioner Hennepin County seek additional Medicare reimbursement to cover indirect costs that HCMC claims were incurred in connection with its graduate medical education program during its 1980 cost year.

In Count I of their Complaint, petitioners requested an upward adjustment of HCMC's 1980 cost limits under 42 C.F.R. 413.30(f)(4) (*see* note 1, *supra*). The district court rejected this claim, holding that petitioners had failed to demonstrate, as explicitly required by that regulation, that any indirect medical education costs incurred in excess of the applicable cost limits were "reasonable, attributable to the circumstances specified, separately identified by the provider, and verified by the [fiscal] intermediary." 42 C.F.R. 413.30(f). Pet. App. 13a-15a.

In Count II of the Complaint, petitioners sought a "retroactive corrective adjustment" under clause (ii) for purported excessive indirect costs of its graduate medical education program. Specifically, petitioners argued that clause (ii) required the Secretary to recalculate HCMC's reimbursement by applying retroactively a recently adopted, revised method for quantifying indirect medical education costs, which had explicitly been made applicable

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grams result in higher reimbursable costs as "compared to other providers in its group." 42 C.F.R. 413.30(f)(4).

to costs incurred by Medicare providers on or after July 1, 1980. See Pet. App. 7a-10a.[2] According to petitioners, the decision to change the method for awarding cost limit exemptions by raising cost limits for teaching hospitals across-the-board "essentially amount[ed] to a recognition that the reimbursement method covering HCMC's 1980 cost year was inadequate" and that application of that method had resulted in insufficient reimbursement for the hospital's graduate medical education costs in 1980. Pet. App. 28a.

With respect to Count II, the district court decided that under the law of the circuit then in effect as set forth in *Georgetown University Hospital* v. *Bowen*, 821 F.2d 750 (D.C. Cir. 1987),[3] clause (ii) did not provide "broad authority for the promulgation of retroactive cost-limit rules." Pet. App. 29a (quoting *Georgetown*, 821 F.2d at 759). The court accordingly found that it was without authority to order the retroactive application of the "teaching adjustment factor" to all providers qualifying under its terms. The court nevertheless concluded that clause (ii) did require a retroactive adjustment "if a *particular* provider demonstrates that *it* was reimbursed inadequately." Pet. App. 30a. The court therefore granted summary judgment for petitioners on Count II, and

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[2] On the basis of a study of the effect of medical education programs on routine hospital costs, the Health Care Financing Administration adopted a "medical education cost adjustment factor," or "teaching adjustment factor" to go into effect beginning July 1, 1980 (which corresponds to HCMC's 1981 cost accounting year). The factor raises teaching hospitals' allowable cost limits by 4.7% for "each increase of .10 in the hospital's ratio of full-time or equivalent interns and residents to its bed size." Pet. App. 8a.

[3] The court of appeals' decision in *Georgetown* was subsequently affirmed by this Court, 109 S. Ct. 468 (1988). See discussion, *infra*.

remanded to the Secretary to "consider whether HCMC itself suffered inadequate compensation." *Id.* at 31a.

On motion for reconsideration and clarification, the district court agreed with the government's contention that, even if petitioners were correct that clause (ii) required a reassessment of their reimbursement amount, the sole method by which HCMC could demonstrate that it individually would be entitled to increased reimbursement under clause (ii) would be through compliance with the terms of the cost limit exceptions regulation, 42 C.F.R. 413.30(f). In particular, the court held that it was incumbent on HCMC to demonstrate that its indirect costs associated with its medical education programs were in excess of those incurred by other similarly situated providers, and that "these costs are separately identified and verified by the intermediary." Pet. App. 37a.

3. The court of appeals affirmed the district court's holding on Count I, ruling that petitioners had failed to show that they were entitled to an exception to the cost limits under the applicable regulation, 42 C.F.R. 413.30(f).[4] However, the court reversed the district court's

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[4] The court rejected petitioners' argument that HCFA's adoption of the "teaching adjustment factor" revealed the inadequacy of previous cost adjustment methods and demonstrated the arbitrariness of the Secretary's refusal to apply the new method retroactively. The court stated, first, that "there is nothing inherently arbitrary or capricious about an agency's decision to apply new data prospectively only." Pet. App. 14a. On the contrary, to embrace petitioners' reasoning "would be to discourage agencies from reconsidering their regulations in light of new data for fear of being forced to apply new regulations retroactively." *Ibid.* Also, the court noted that petitioners had challenged "neither the legality of the standard under 42 C.F.R. [413.30(f)], nor its applicability to this case," and that HCMC clearly had failed to qualify for an exemption or retroactive adjustment under the regulation. Pet. App. 14a. Since HCMC had failed to comply with a reasonable and lawful requirement that it " 'separately identif[y]' its

order remanding for further consideration under clause (ii). Relying on this Court's decision in *Bowen* v. *Georgetown University Hospital*, 109 S. Ct. 468 (1988), the court of appeals expressly rejected petitioners' assertion that clause (ii) provided an independent vehicle for determining entitlement to reimbursement, wholly apart from the methods for computing cost limits (or for establishing entitlement to exemptions from costs limits) as set forth in the Secretary's regulations implementing 42 U.S.C. 1395x(v)(1)(A) (1982 & Supp. V 1987). Pet. App. 15a-16a.

In so holding, the court of appeals noted that this Court had interpreted clause (ii) and its implementing regulations[5] as providing for "adjustments only to the *aggregate amounts* of reimbursement pursuant to valid regulatory methods; they do not permit changes in the *methods* used to compute costs." Pet. App. 16a (citing *Georgetown*, 109 S. Ct. at 473 & n.2). The court explained that the purpose of clause (ii) is "to ensure that petitioners receive what they are actually *due* under the applicable regulation, no more and no less" (Pet. App. 17a). Thus, the court held, clause (ii) authorizes only case-by-case recomputation (or "book balancing") of the amount of reimbursement due a provider using the prescribed procedures for calculating costs

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costs warranting a claim for a medical education exception," the decision to deny a retroactive adjustment "was neither arbitrary, capricious, nor an abuse of discretion." *Id.* at 15a. Petitioners do not seek further review of the court of appeals' denial of relief under 42 C.F.R. 413.30(f) in Count I of the Complaint.

[5] The Court in *Georgetown* pointed out that the provision for retroactive adjustment under clause (ii) was implemented by regulations, 42 C.F.R. 405.451(b)(1), 405.454(a) and (f) (1985). It characterized these regulations as "provid[ing] for adjusting the amount of interim payments received by a provider, to bring the aggregate reimbursement into line with the provider's actual reasonable costs." 109 S. Ct. at 473.

(including the regulations governing the determination of cost limits and the application of exemptions); it does not mandate the retroactive application of any new methods for calculating costs. Accord, *Daughters of Miriam Center for the Aged* v. *Mathews*, 590 F.2d 1250, 1258 n.23 (3d Cir. 1978).

ARGUMENT

Petitioners contend that the judgment below is in "direct conflict" with decisions of other courts of appeals, and that "[t]his split among the circuit courts creates conflict and confusion in the administration of the Medicare Act." Pet. 6. However, this Court's decision in *Georgetown* supersedes inconsistent prior opinions of the courts of appeals and resolves any "confusion" that may previously have existed concerning the issue in this case: whether clause (ii) requires the retroactive application of new regulatory methods for calculating the amount of reimbursement due a provider. Since the court of appeals in this case properly applied the teachings of *Georgetown*, further review by this Court is unwarranted.

1. a. In *Georgetown*, this Court rejected the Secretary's argument that clause (ii) authorized the Secretary to recover excessive reimbusement through the retroactive application of a new method for determining reimbursable costs.

In clarifying the scope of clause (ii), the *Georgetown* Court explained that clause (ii) "directs the Secretary to establish a procedure for making case-by-case adjustments to reimbursement payments," 109 S. Ct. at 472, and that 42 C.F.R. 405.451(b)(1), 405.454(a) and (f) (1985) were "intended to implement the Secretary's authority under clause (ii)" by setting forth the method established by the Secretary

for such accounting reconciliation.[6] 109 S. Ct. 473 n.2. The Court further ruled that "nothing in clause (ii) suggests that it permits changes in the *methods* used to compute costs; rather, it expressly contemplates corrective adjustments to the *aggregate amounts* of reimbursement produced pursuant to those methods." 109 S. Ct. at 473.

Petitioners assert that *Georgetown* only presented the question whether clause (ii) authorized the Secretary to apply new cost accounting methods retroactively to recover excessive costs from providers, and that this Court in *Georgetown* "did not * * * attempt to define the precise contours" of clause (ii) in its application under the circumstances presented here. Pet. 7. This contention does not withstand scrutiny. Although the question presented in *Georgetown* was whether clause (ii) *permits* the retroactive application of new rules to recapture excessive reimbursement—not whether that section *mandates* retroactive application to increase deficient reimbursement to the provider—the Court in *Georgetown* effectively addressed the second question in the course of answering the first. In rejecting a construction of clause (ii) that would allow for the retroactive promulgation of cost limit rules, the Court

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[6] These regulations "provide for adjusting the amount of interim payments received by a provider, to bring the aggregate reimbursement into line with the provider's actual reasonable costs." 109 S. Ct. at 473. Section 405.451(b)(1) (1985) specifically provides for

> the making of suitable retroactive adjustments after the provider has submitted fiscal and statistical reports. The retroactive adjustment will represent the difference between the amount received by the provider during the year for covered services * * * and the amount determined in accordance with an accepted method of cost apportionment to be the actual cost of services rendered to beneficiaries during the year.

See also 109 S. Ct. at 473 n.2

made clear that clause (ii) "speaks in terms of adjusting the aggregate reimbursement amount computed by one of the methods of determining costs;" it does not permit the Secretary to change retroactively the "*methods* used to compute costs." 109 S. Ct. at 473.

In contending that clause (ii) requires the Secretary to apply the method established for 1981 to costs incurred by HCMC in 1980, petitioners would have this Court ignore the foregoing statement in *Georgetown*. If, as *Georgetown* holds, clause (ii) does not authorize the Secretary to promulgate a retroactive change in methodology to recover "excessive reimbursement," then clause (ii) cannot authorize such a retroactive change in methodology to remedy alleged "deficient reimbursement." Providers in such circumstances are confined to the Secretary's "exceptions" process under the regulations established by the Secretary for that purpose. And if clause (ii) grants the Secretary no authority to make a retroactive change in the method for calculating reasonable costs, then surely it would be illogical to conclude that the same provision *requires* that the Secretary make a retroactive change in the method as applied to individual providers.[7]

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[7] As we noted in our brief in *Georgetown*, "retroactive rules are authorized by Clause (ii) in either both 'inadequate' and 'excessive' reimbursement cases, or in neither circumstance." Br. for the Pet. at 47 n.41. Thus, providers cannot have it both ways. If the Secretary may not, as *Georgetown* holds, apply regulations retroactively to recover "excessive reimbursement," providers may not insist on a retroactive application of a regulation so as to allow the provider to recover allegedly "inadequate reimbursement."

Consequently, applying the 1981 cost limits rule retroactively to HCMC's 1980 cost year would constitute precisely the retroactive change in methodology prohibited under *Georgetown*. Pet. App. 17a. The court of appeals was therefore correct to hold that petitioners' only remedy for the alleged inadequate reimbursement for HCMC's 1980 cost year was to meet the requirements of the "exceptions" process set forth in 42 C.F.R. 405.30(f). As the district court and the court of appeals both held, it was precisely the requirements of this regulation that petitioners in this case failed to satisfy.

b. Given the intervening decision in *Georgetown*, it is of no consequence that the interpretation of clause (ii) enunciated by the court of appeals below runs counter to the construction accorded clause (ii) by the Second, Eighth, Ninth and Eleventh Circuits. Each of the decisions discussed by petitioners was rendered prior to *Georgetown*, and each court of appeals read clause (ii) as requiring the retroactive adoption of a new method of calculating reimbursement where previous cost calculation methods allegedly failed adequately to reimburse a provider. Thus, each decision suffers from the basic flaw of requiring the Secretary to make retroactive changes in the method of calculating reasonable costs under the Medicare Act. See *Kingsbrook Jewish Medical Center* v. *Richardson*, 486 F.2d 663 (2d Cir. 1973); *St. Paul-Ramsey Medical Center* v. *Bowen*, 816 F.2d 417 (8th Cir. 1987); *Regents of the University of California* v. *Heckler*, 771 F.2d 1182 (9th Cir. 1985); *Medical Center Hospital* v. *Bowen*, 839 F.2d 1504 (11th Cir. 1988).

Petitioners assert (Pet. 13) that the *Georgetown* Court "did not express an opinion as to the appropriateness" of the interpretation of clause (ii) adopted in these decisions. However, after noting the courts of appeals' varying interpretations of clause (ii), the *Georgetown* Court definitively embraced the year-end reconciliation interpretation of that provision adopted by the Third Circuit in *Daughters of Miriam Center for the Aged.* It correspondingly rejected the view that clause (ii) authorized retroactive rulemaking, and thereby implicitly repudiated the circuit court decisions construing clause (ii) as authorizing or requiring the retroactive application of new cost calculation methods. Thus, the decision in *Georgetown* resolved any conflict in the circuits on the issue presented here.

2. Petitioners are in error in asserting that the court of appeals' construction of clause (ii) would render it superfluous because 42 U.S.C. 1395g (1982 & Supp. V 1987) already "provides for the periodic estimated payments and adjustments that [the Third and D.C.] circuits refer to in their respective discussions of [clause (ii)]." Pet. 11. As explained by the Third Circuit in *Daughters of Miriam Center*, 590 F.2d at 1258 n.23, Section 1395g(a) requires the Secretary to make periodic interim estimated payments "not less often than monthly" and "prior to audit or settlement" at the close of the provider's fiscal year. The adjustments mandated under Section 1395g(a) therefore have the limited aim of ensuring that each periodic interim payment accounts for any "previously made overpayments or underpayments" (*ibid.*).

In contrast, clause (ii) authorizes a final retroactive corrective adjustment as part of a year-end audit and settlement that takes into account overpayments or underpayments incurred following the final periodic interim payment. Thus, Section 1395g and clause (ii) work in tandem to guarantee that interim estimated payments to

providers under Section 1395g are "in line with the amount actually due them under the annual audit." *Daughters of Miriam Center*, 590 F. 2d at 1258 n.23.

3. Petitioners acknowledge that *Georgetown* forecloses any general retroactive application of a new method—including the "teaching adjustment factor" adopted by the Secretary in 1981—for use in calculating the amount of reimbursement due a provider. See Pet. 14. Petitioners appear to take the position, however, that it would not be inconsistent with *Georgetown* to interpret clause (ii) as requiring that a provider be permitted to demonstrate, on a case-by-case basis, that existing methods for calculating reasonable costs do not adequately account for actual reimbursable costs. See, *e.g.*, *St. Paul-Ramsey Medical Center* v. *Bowen*, 816 F.2d 417 (8th Cir. 1987); *Regents of University of California* v. *Heckler*, 771 F.2d 1182 (9th Cir. 1985).

However, insofar as petitioners' construction of clause (ii) necessarily entails a "*post hoc* reassessment of the efficacy of the relevant standard" for calculating the appropriate amount of reimbursement in each case, Pet. App. 17a, it cannot be reconciled with *Georgetown*, which holds that clause (ii) authorizes no such reassessment. And to the extent that petitioners' position contains an implicit attack on the "adequacy" of existing methods in fixing the reasonable cost amount, it is inconsistent with petitioners' acknowledgment before the court of appeals that the existing method for determining whether an individual provider would be entitled to an upward adjustment of its reimbursement for education expenses, as set forth in 42 C.F.R. 413.30(f), was a valid and "lawful" procedure and was fully applicable to HCMC's claim.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

Respectfully submitted.

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* The Solicitor General is disqualified in this case.

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